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C O N F I D E N T I A L SECTION 01 OF 02 VILNIUS 000512

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E.O. 12958: DECL: 06/01/2016
TAGS: ENRG ECON EPET PREL PGOV LT RS
HT9
SUBJECT: PARLIAMENT APPROVES AGREEMENT TO SELL LITHUANIA'S
OIL REFINERY TO POLISH COMPANY

REF: A. VILNIUS 459 AND PREVIOUS

¶B. VILNIUS 285
¶C. WOODARD-GERMANO E-MAIL 5/26
¶D. WARSAW 980

Classified By: Economic Officer Scott Woodard for reasons 1.4 b and d

SUMMARY

¶1. (C) Lithuania's parliament on June 1 approved the sale of Lithuania's Mazeikiu Nafta (MN) oil refinery to the Polish oil company PKN Orlen. Next, the EU's competition authority must approve the deal, a process that could take months. With the question of the next owners now answered, MN will focus on securing future crude supplies. A critical financial assumption of the deal is that world oil prices will remain high for years, enabling the refinery to remain profitable even if Russian supplies are cut off and oil must be brought to the refinery by sea. The Polish deal has evoked widespread relief among Lithuanians, who hope it will herald improved economic relations with Poland, particularly in the export of surplus electricity. END SUMMARY.

PARLIAMENT APPROVES SALE OF REFINERY

¶2. (U) Lithuania's parliament on June 1 approved by a vote of 97 to 1, with 7 abstentions, the four documents that will enable the sale of MN to PKN Orlen to go forward. The Acting Minister of Economy will reportedly sign the four documents on behalf of the GOL on June 6. These four documents comprise a new shareholders' agreement, an agreement to sell the GOL's 30.66 percent stake in MN, a put option allowing the GOL to sell the rest of its MN shares to PKN Orlen, and a deed canceling earlier agreements with Yukos and Williams International. (NOTE: The U.S. oil company Williams International sold its majority ownership of MN to Yukos in ¶2002. Yukos agreed last week to sell its 53.7 percent stake in MN to PKN Orlen after the judge in the Chapter 15 bankruptcy case in New York lifted the temporary restraining order that had prevented Yukos's executives from signing a deal. END NOTE.) PKN Orlen will reportedly pay the same per-share price to both Yukos and the GOL, with Yukos receiving USD 1.492 billion for its shares, and the GOL USD 851 million.

NEXT STEPS: SIGNATURES, EU APPROVAL

¶3. (C) Saulius Specius, advisor to former Prime Minister Brazauskas and one of the GOL's main negotiators on the MN sale, told us on June 2 that the GOL will decide on June 5 whom to assign signing authority. He expects the GOL to empower acting Minister of Economy Dauksys and that the signing will take place on June 8 or 9. Specius said that the government's June 1 collapse should have little effect on the signing of the agreements.

¶4. (C) The European Commission's Directorate-General for Competition (DGC) must approve the deal, a process that will likely take months. Specius told us that the DGC would normally take three to four months to issue a ruling on a case like this. He added, however, that the GOL planned to encourage the DGC to issue a decision more expeditiously. MN's Amcit Managing Director, Nelson English, told the Ambassador on May 30 he is concerned that significant delay by DCG will provide ample opportunity for Russian intrigue in the interval.

CRUDE: BY LAND OR BY SEA?

¶5. (C) English told the Ambassador that MN had commissioned a study to determine the feasibility of MN's crude oil supply options. This study, which assumes crude prices of USD 70 as the norm until 2010, concluded that MN will remain profitable, even if it has to get its crude supplies solely

by tanker via its Butinge terminal on the Baltic Sea. During a May 25 visit to MN, the refinery's senior managers told us that obtaining crude via tankers loaded in Rotterdam adds about USD 20 per barrel to the cost of supply. The Butinge terminal's 10-million tons/year intake capacity is sufficient to provide annual supplies to the refinery. (NOTE: The refinery processed 9.2 million tons in 2005 and management expects to be able to refine slightly more than 10 million tons when it completes its modernization upgrades over the next three to five years. END NOTE.)

¶6. (C) English told the Ambassador that he continues to pursue a supply agreement with Venezuela's state-owned PDVSA, although he was not optimistic about concluding an agreement (ref B). English reiterated that any agreement with Venezuela will include an escape clause that would allow MN to break the contract should Venezuela use this supply arrangement to redirect supplies of crude away from the United States. English said that the he was also considering supply possibilities from Libya and Yemen.

¶7. (C) The feasibility of sea-freighted oil aside, MN's senior managers told us that they expect Russia to continue to supply crude via pipeline to MN. They recognize that Russia can, for political reasons, cut its supply of crude to MN, but reason that Russia is pumping oil out of the ground faster than it can export it. Cutting off one of its export routes simply will not make economic sense. Russia continues to export crude via Butinge, they say, because it needs the export capacity.

COMMENT: AN END IN SIGHT?

¶8. (C) The 16-month saga of the sale of MN may -- finally -- be nearing its conclusion. Rumors and speculation about continued Russian attempts to scuttle this deal in favor of Rosneft or another Kremlin favorite will undoubtedly persist. We think it is significant that the Parliament's

overwhelming approval of the deal came on the same day that Prime Minister Brazauskas submitted his resignation to President Adamkus. This seems to disprove the theory circulating here that this week's political turmoil was a smokescreen to prevent the refinery from falling into Polish hands. Despite all of the turmoil in Lithuania's political scene, it appears that the deal will hold.

¶9. (C) There is widespread relief across the political spectrum here that for now Lithuania has succeeded in diversifying its domestic energy industry. An added benefit to the Orlen deal is that it will substantially fortify Lithuania's economic relationship with Poland, and possibly open the door to greater cooperation between the two neighbors in enhancing European energy security. The Lithuanian government in particular hopes the Polish government will increase its receptivity to cooperating in building an "electricity bridge" with Poland in order to facilitate exporting Lithuania,s surplus westward.tinge terminal just might get the opportunity to demonstrate their ability to offload crude.
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